

technological state of the art at the time. All services were cablecast, undifferentiated, and provided to all subscribers. The systems were rebuilt periodically and upgraded over time to increase channel capacity, upgrade amplifiers, enhance headends, become addressable add earth stations, overlash fiber, install underground fiber vaults, add self-healing rings, and so forth. Each step required substantial material and labor costs, all necessary at the time, but only some of which would be expended were we to build a system from scratch in unserved territory today. Nor could any operator economically build such a system today, even theoretically, because today there is no significant unserved area. As a result, the cost of building such an "ideal" system today, in order to leapfrog technological evolutionary steps, is more than twice the cost per-home than one would theoretically incur, because one's market share is substantially limited by the power of an incumbent efficiently operating a cable system as a going concern. In short, however theoretically "inefficient" it might appear for the industry to have evolved over time, that evolution was necessary for cable operators to be in the position today to serve the public.

### 3. Reproduction Cost

The cost of reproducing an old technology system really makes no sense in determining the value of the capital committed to the enterprise. First of all, calculations as to various

costs of obtaining and using technologically obsolete equipment is itself inherently subject to inaccurate predictions. Moreover, because these particular costs are for establishing tangible assets, they would naturally fail to reflect the necessary capital which must be committed to a new build in sustaining start-up losses and foregone earnings through the initial years of deployment and development. Rather than undertaking this useless exercise, a more appropriate market value approach or one which recognizes the necessary capital committed or other "intangibles" better reflect a starting point of bringing a new industry into regulation.

#### H. Other Rate Base Issues

##### 1. Excess Capacity

The Commission suggests that an allowance for plant costs might be limited due to "excess capacity." (NPRM ¶¶ 42-43). In fact, the channel capacity of cable systems today are not "excessive;" if there is capacity, it is because systems are upgraded in "lumps." One can add 16 channels (upgrade from 450 MHz to 550 MHz) for the same cost as adding 5 channels -- indeed, it is difficult to find equipment that does not jump in large increments of capacity. Moreover, because labor costs for the upgrade would be the same, it may be "imprudent" not to add excess capacity.

Similarly, fiber deployment entails the same (capitalized) labor charges if there are 24 strands in the sheath or if there are 12. The fact that not all channels are immediately programmed is a tribute to cable operators' planning, and their efforts to retain capacity for new programmers like must carry shopping networks, leased access users, and new cable networks seeking access to cable audiences.

In addition, all of the plant is powered. The headend, with perhaps the addition of some modulators, is fully functional and in service. All of the cable plant in service could be used to provide service to subscribers on a short-run basis if sufficient demand existed to consume the capacity now held in reserve. By contrast, telco equipment loop utilization factors have been declining persistently since divestiture.<sup>63/</sup> Considering that the Commission and Congress seek to encourage the deployment of new technologies, it would be inconsistent for the Commission to disallow investment in channels presently held in reserve.

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<sup>63/</sup> Although telco deployment of fiber has increased annually since divestiture, the number of circuits that can be multiplexed onto the same fiber changes as terminal and repeater technologies improve. Therefore, the same underlying fiber data from prior years can be updated to estimate maximum available capacity. For example, new terminal technology supports almost 25,000 two-way circuits on a single fiber pair, more than triple the capacity of earlier systems. Because carriers are acutely aware that upfront costs for fiber deployment in absolute terms are high, a significant portion of the total investment can be deferred until demand materializes. FCC Fiber Deployment Update -- 1992 (Released April 30, 1993) at 2.

## 2. Working Capital

Working capital is traditionally defined as follows:

The average amount of capital provided by investors in the company over and above the investment in plant and other specifically identified rate base items, to bridge the gap between the time expenditures are required to provide service and the time revenues are received for that service.

Hahne, et al., Accounting for Public Utilities, p. 5-2 (Matthew Bender 1984).

Components of working capital are generally material and supplies inventories, prepayments and cash working capital. A thirteen-month average of materials and supplies is typically used in the utility industry to reflect that investors must fund the materials and supplies necessary to provide service on a daily basis. Materials and supplies usually is a non-controversial item and has been approved as a working capital component by the FCC.<sup>64/</sup> Prepayments are made in advance of the period to which they apply and include such items as insurance and taxes.

Cash working capital usually garners the most attention and has been controversial because three different methodologies

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<sup>64/</sup> See Amendment Of Part 65 Of The Commission's Rules To Prescribe Components Of The Rate Base And Net Income Of Dominant Carriers, 4 F.C.C.Rcd. 1697, 1702 (1989).

have developed and been used by regulatory agencies: the lead-lag study, balance sheet approach, and formula methodology. It would be appropriate for the FCC to adopt the formula methodology to provide cable operators cash working capital needed to pay operating expenses and maintain appropriate cash balances.

It is generally agreed that the lead-lag study is the most accurate cash working capital methodology. A lead-lag study, in excruciating detail, measures the time between (1) the time service is rendered until revenues for that service are received, and (2) the time that labor and materials used in providing service are incurred and recorded and paid for. An accurate lead-lag study is time-consuming, complicated and expensive to conduct.

The balance sheet approach typically entails a comparison of assets and liabilities. As a measure of cash working capital, the balance sheet approach is fatally flawed. If current liabilities exceed current assets, the balance sheet methodology would produce a conclusion that there is no need for cash working capital. Taken to its logical extreme, a company on the verge of bankruptcy has no need for cash working capital.

The balance sheet methodology is also improper for estimating cash working capital needs because it provides only a snapshot view of a company's financial picture. Cash working capital requires a dynamic determination to establish daily needs

of the company to pay ongoing expenses before revenues are received for services rendered. The balance sheet approach only explains where one is at a specific time, not how one arrived there or what was needed to reach that destination.

The formula methodology developed as a reasonable proxy of lead-lag study results without the exorbitant expense, hearing time and controversy involved in reviewing the detailed, controversial study. As the name implies, the formula methodology calculates  $1/8$  of operation and maintenance expenses (45 days divided by 365) for cash working capital requirements.

The FERC utilizes the formula methodology, recognizing its validity and ease of use.<sup>65/</sup> The FCC considered cash working capital methodologies Amendment Of Part 65. After approving the lead-lag study in its initial 1987 order,<sup>66/</sup> the FCC reconsidered its propriety and adopted the formula approach, recognizing that cost savings warranted the slight reduction in precision achieved. Although the FCC has approved the lead-lag study approach to cash working capital in interstate carrier cases, cable operator regulation is intended to be less cumbersome and technical than interstate carriers.

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65/ See, e.g., Middle South Energy Inc., ER82-616-000, 1984 FERC LEXIS 3396 (1984).

66/ Amendment of Part 65, 3 F.C.C. Rcd. 269 (1987).

Clearly, the FCC has expressed interest in streamlining the cost of service option under cable operator regulation. The formula approach is consistent with that goal, utilized by other regulatory agencies, adopted in the past by the FCC and should also be adopted for cable operators.

### 3. Accumulated Deferred Taxes

Accumulated deferred taxes should not be deducted from the ratebase. These deferred taxes arise because of the difference in the timing of certain expenses between book (GAAP accounting) and income tax accounting. The primary timing difference is often due to the more accelerated depreciation allowances in the Internal Revenue Code than is allowed in book accounting. The difference between the depreciation expense for books and the depreciation expense for taxes times the tax rate is usually the major component of income taxes deferred.

In a regulated environment, deferred taxes represent cost-free capital. Customers supply this capital mainly in the form of the revenue requirement for depreciation and tax expense which are built into the rates they pay for regulated service. The customer, in effect, pays book depreciation and tax expense, while the regulated firm is allowed to deduct a larger amount of depreciation expense on its tax return, resulting in a lower tax payment. This temporary difference in tax payments is generally considered to be an interest-free loan from the government and is usually deducted from ratebase.

In a non-regulated environment, prices are not set on a cost of service basis and there is no rationale for arguing that a customer has in effect made a loan to the firm. In the current instance, cable TV companies only recently have been subject to price regulation. The deferred taxes on the books of cable TV firms accumulated during a time when these firms were not regulated and therefore there is no basis for deducting the current balance of deferred taxes from ratebase.

As an example, in KBLCOM's specific case, rates do not cover its costs as reflected in its historical financial statements.<sup>67/</sup> Of course, rates do generate income from operations. However, after paying interest and amortizing intangibles, no net income results. If customer rates had contributed customer supplied capital, KBLCOM's financial position would reflect some positive earnings, instead of its current \$500 million in negative retained earnings. Exhibit A.

#### 4. Depreciation

"Depreciation accounting" purports to balance capital consumption against capital revenues by spreading an asset's

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<sup>67/</sup> These statements were discussed previously with regard to KBLCOM's "negative" net worth due to deficiencies in the retained earnings accounts. See Exhibit A. These deficiencies arose -- and continue to accrue -- because the rates charged do not reflect, yet alone recover -- all the costs incurred in providing cable service.



depreciation costs over its useful life. "It serves to distribute equitably throughout the several years of service life the only expense of plant retirement which is capable of reasonable ascertainment -- the known cost less the estimated salvage value.<sup>68/</sup> In essence, depreciation accounts for the loss of service value of a capital asset as a result of wear and tear as well as technological obsolescence.<sup>69/</sup> Regulated common carriers can recover depreciation dollar for dollar as an element of their expense items to be added in the calculation determining revenue requirements.

Pursuant to Commission practice, LECs submit triennial depreciation rate studies utilizing historical analysis and predictions as to future technological developments to establish depreciation rates for particular accounts and overall composite rates for the entirety of the telephone company's plant. Joint Commenters generally concur with the Commission's view that the remaining life method is the most appropriate means of depreciating cable plant, but putting cable into the same telco triennial regime would be of no value whatsoever.

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<sup>68/</sup> Louisiana Pub. Serv. Comm'n v. F.C.C., 476 U.S. 355, 364 (1986).

<sup>69/</sup> 47 C.F.R. §32.9000 (defining depreciation); Louisiana Pub. Serv. Comm'n, 476 U.S. at 364 (1986).

Calculating remaining life for cable is extremely difficult today. Cable television is in the midst of three simultaneous revolutions: (1) the conversion from analog to digital signalling, (2) the transition from coaxial cable to fiber, and (3) the renewal of the vast bulk of franchises issued during the late '70s and early '80s. Cable assets must be reevaluated periodically to determine if the expected useful life of an asset has changed, not just due to physical obsolescence but due to technological obsolescence as well. Long amortization periods typically associated with GAAP are premised on the accounting assumption that the business will continue in perpetuity. The assumption may have been appropriate for utilities and telephone companies, who operate under certificates of compliance which are virtually perpetual. They are hardly applicable to cable television franchises, which are typically for 10-15 years, and carry with them the risk of non-renewal and the near-certainty that the conditions of renewal will be technologically demanding.

Other fundamental characteristics of the cable industry preclude easy reliance on telephone depreciation prescriptions. Cable places heavy reliance on customer premises equipment. Converters are an integral part of the transport structure because they enable cable operators to make use of distribution bandwidth which is otherwise not receivable by older receivers, and to upgrade to greater channel capacity without awaiting the relatively long (7 - 15 year) replacement cycle of embedded television receivers.

Most operators are expecting analog converters to be replaced shortly by digital decompression boxes. In addition, we expect that with the adoption of equipment compatibility standards along the line of the NCTA/EIA accord, combination converter/decoders will be phased out in favor of standalone decoders. For these technological reasons, the existing base of CPE must be more rapidly depreciated than originally expected.

Accounting for these unique factors is further complicated by the variation in treatment among operators. Most (not all) cable operators follow GAAP for accounting records, but do not follow the detailed account practices characteristic of the USOA. Thus, for example, it is commonplace for converters of different types, held for different classes of service, to be held in a single mass account. Each type of converter has been depreciated over the appropriate number of years, but it is a difficult job to reconstruct the accumulated depreciation associated with only one type of converter.

At present, there is no immediate means for translating all cable television depreciation records into an "official" accounting system. The depreciation practices of cable operators vary widely. Depending on the technologies employed by a particular operator, age of the system, or other individual mortality characteristics, depreciable lives vary widely among companies even within the same plant account. Therefore, the prescribed

rates or range of rates for each plant account will likely vary among systems and even in some cases within systems. It would take several years for the Commission to accumulate enough data to prescribe depreciation rates by class of plant, as it has with the telcos.

Requiring the industry to go through the complex depreciation processes currently utilized by the LECs is not warranted. Substantial expenditures for completing the studies and implementing depreciation rates are clearly not justified in the cable industry.<sup>70/</sup> To that end, the Commission proposed to simplify the depreciation prescription process for LECs and eliminate the need for the expensive and detailed studies and allow significant flexibility in determining and applying depreciation rates.<sup>71/</sup> Because the cable industry does not have the history of this process or the accumulated data concerning projection lives, survivor curves, salvage values and the like, even three of the four options proposed for the LECs will not be helpful. Those options still require the Commission to establish a range of basic factors based on parameters derived over the past years or establishing a particular schedule for each plant account. Due to the inconsistencies in each cable operator's accounting

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<sup>70/</sup> Telephone common carriers estimate that as much as \$50 million is spent annually to determine depreciation rates for their industry.

<sup>71/</sup> NPRM 9926-27.

practice, and the absence of industry-wide data, these types of initiatives would be as problematic as commencing depreciation analysis with the use of historical studies and mortality predictions.

However, the fourth option offered to communications common carriers (the price cap carriers) would allow the particular carrier to file depreciation rates with no supporting data, but allow the public to comment on the proposed rates. In much the same manner that franchising authorities would be able to review basic rates and subscribers allowed to file complaints, the Commission could review depreciation practices as required by the circumstances.<sup>72/</sup>

Accordingly, given the fact that revolutions of digitization and fiberization, as well as franchise renewals will be occurring at the same time as the Commission would seek to complete an enormously complex depreciation study, it is far better for the Commission to accept current depreciation practices. This should present no significant risk. Many operators' depreciation expenses have been subjected to routine review by outside auditors for compliance with GAAP, by the SEC in public filings, and review by potential investors. There has been no motive or

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<sup>72/</sup> It should be noted that, unlike the situation for LECs, the Commission is not under an obligation to prescribe depreciation rates for cable. Compare 47 U.S.C. § 220(b) with 47 U.S.C. § 623.

opportunity to overstate depreciation expenses. Accordingly, present depreciation rates should be entitled to a presumption of reasonableness, with the Commission's retaining the authority to monitor results and to correct rates for observed abuse.

#### IV. CALCULATING THE RATE OF RETURN

The appropriate rate of return method for the cable industry must satisfy two fundamental needs: first, it must fully account for the differences between cable and telephone financing; second, it must guarantee investors the opportunity to be appropriately compensated on a current basis. As set forth in the attached AUS analysis, the Commission should establish 18.9% as the pre-tax overall rate of return. AUS Report at 59-85.

Joint Commenters understand the intense time pressures on the Commission and the temptation to borrow heavily from telephone precedent in establishing the return element. Unfortunately, the financial characteristics of the cable industry preclude wholesale importation of the methodology previously used to establish telephone return. On the fundamental level of comparability, the telephone industry resembles cable, principally because it has capital intensive plant hanging on utility poles. But beyond that, the risks associated with cable firms are considerably greater than those associated with an investment in an LEC.

**A. DCF Methodology**

DCF or, discounted cash flow, was suggested by the Commission as a method for calculating the rate of return for cable companies. The DCF method presumes that the price of a share of stock is equal to the present value of the cash flow as the stock will generate. Because these cash flows are in the form of "dividends", any company that does not have current earnings or is not paying dividends will "flunk" the DCF methodology without recognizing that investors still expect equity appreciation. Because investors in cable stock receive a fundamentally different "return" on their investments as opposed to investors in telco stocks, the DCF methodology does not produce a rational result.

First, cable firms remain relatively immature. Cable's overall performance demonstrates almost universal absence of dividends.<sup>73/</sup> By contrast, RBOCs and GTE are larger, more mature and have routinely made current earnings and paid dividends for the pertinent history of ratemaking.

Moreover, cable firms are less diversified than telephone companies. The typical RBOC holds interests in real estate, and owns properties over a vast geographic area, spreading risk across lines of business and the world. For

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<sup>73/</sup> Exhibit D, Table 3.

example, Southwestern Bell's subsidiaries, in addition to traditional communications services such as land-line and wireless telecommunications, sell advertising for and publish Yellow Pages and White Pages directories; provide customer premise equipment, private business exchange and cellular equipment; sell paging services; and even cable television. Southwestern Bell's traditional telecommunications services include local services, network access, dedicated private line and toll services. Southwestern Bell also owns interests in directory, cable television and telecommunications businesses in Australia, Israel, Mexico and the United Kingdom.<sup>74/</sup>

Bell Atlantic Corporation, the parent of seven telephone subsidiaries (network services companies), provides another example. Bell Atlantic's network services companies' lines of business include the traditional local exchange services, private line, and customer premises services such as inside wire installation and maintenance, as well as cellular mobile service; servicing and repairing computers; and providing software for telecommunications and computer networking, leasing commercial, industrial, medical and high technology equipment, real estate investment and development; and sale and distribution of

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<sup>74/</sup> See 1992 Annual Report of Southwestern Bell Corp., Form 10-K, Securities and Exchange Commission, No. 1-8610. Southwestern Bell reached an agreement to sell its paging services in mid-1993, subject to regulatory approval.



liquified petroleum gas.<sup>75/</sup> By contrast, most cable companies are specialized in one line of business: distribution of video entertainment. One objective measure of the greater risk of cable investments compared with telephone are the comparative beta factors. Beta measures the level of changes of a firm's stock in comparison to overall changes in the market, as a means of isolating the risk associated with investment in that firm as opposed to the general risks associated with the market. The beta for publicly traded cable firms is more than 1.3, compared with less than 1.0 for telephone.<sup>76/</sup> This objectively demonstrates the greater risk associated with cable investments compared with telephone and is not a surprising result. Cable companies are relatively small do not have long successful financial track records. Companies with that kind of profile are relatively risky investments vis a vis telcos and the market in general, thus producing a Beta over 1.

Another objective measure of risk is market share. We will assume that cable has market power, as does telephone. But market power is relative: cable's market share is only 60%, compared with telephone's 95%. Market share is an accepted measure of relative market power. It is obviously a different risk

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<sup>75/</sup> See Annual Report of Bell Atlantic Corp., Form 10-K, Securities and Exchange No. 1-8606.

<sup>76/</sup> AUS Report at 70-71.

proposition to operate a firm with 60% market share, against competition from other sources of information and entertainment, than it is to operate the only local exchange with insignificant present competition. Thus, at the fundamental level of economic evidence, investment in cable firms is far riskier than investment in LECs. Any return must account for that premium.

The following chart demonstrates an approach to calculating a "cable" return reflecting the degree of increased risk associated with cable over telco.

# REGULATED TELCO RETURNS ON INVESTED CAPITAL SET BY FCC

Year	(after tax) Return	Marginal FIT	(pretax) Return & Tax Factor	Cable Risk Differential Basis Pts	Cable PT ROR Via FCC	Note
1983	11.75%	0.46	0.2176	350	0.2824	FCC Dkt 79-63
1984	11.75%	0.46	0.2176	350	0.2824	
1985	12.75%	0.46	0.2361	350	0.3009	FCC Dkt 84-800
1986	12.75%	0.34	0.1932	350	0.2462	
1987	12.00%	0.34	0.1818	350	0.2348	
1988	12.00%	0.34	0.1818	350	0.2348	
1989	12.00%	0.34	0.1818	350	0.2348	
1990	11.25%	0.34	0.1705	350	0.2235	FCC Dkt 89-624
1991	11.25%	0.34	0.1705	350	0.2235	
1992	11.25%	0.34	0.1705	350	0.2235	

\*In the 1986-90 period cable yields averaged almost 500 basis points above telco so 350 basis points is conservative.

## **B. AUS Proposed Rate Of Return**

A fundamental requirement of establishing a return is to assure a present opportunity to earn the authorized return. The traditional regulatory practice has been to calculate a cost of capital using embedded cost of debt, preferred stock and an estimated cost of equity for the specific firm. Traditional methodologies lose their value, however, when a major portion of the industry does not pay dividends, reflect positive operating income, or have investment grade securities. Other approaches therefore are essential to calculate an overall rate of return permitting cable operators to attract capital on reasonable terms, and to maintain financial integrity. Comparable industries at times have been used for the cost of equity when direct examination of equity costs is not possible. Of course, developing a true comparable set of companies or industries is a difficult endeavor but, it is a useful tool when traditional methodologies fail and one that should be explored in this context.

AUS has detailed a comparable earnings alternative for determining rate of return in its recommendations, ultimately including that rates in the 18-19% range would be appropriate. Included in its decision, AUS identifies a number of candidate comparable groups for the Commission's consideration. Selection of the candidates groups is the key ingredient of any comparable

earnings approach and must be considered part of the threshold determination to use that methodology. Simply stated, should the Commission decide that comparable earnings is appropriate it must at the same time establish whether a truly comparable group exists. And cable operators must be permitted an opportunity to explore the reasonableness of the group selected. For if the group is not comparable, another methodology may be more appropriate than fruitlessly searching for "another group." Thus, the FCC could adopt comparable earnings if the groups as specifically recommended by AUS are selected. If that particular selection is not made, the rule should not specify that comparable earnings shall be the rate of return methodology for all cost-of-service showings because it may be more feasible to utilize another methodology such as risk premium, than find an acceptable, comparable group.

In any event, one may not use an "investment cycle" approach, however, to measuring rates of return and other financial performance without sacrificing the fundamental requisite for compensation: the opportunity to earn a current return. If the Commission were to establish a return which assumed that the rate of return might eventually be recovered, all current rates would be depressed at the very point in cable's investment when past losses are due for recovery. If the Commission were in a position to guarantee that a future return higher than the prescribed level would be assured over the investment cycle, it

might be able to adopt an investment cycle approach. However, the Commission cannot provide such a guaranteed opportunity, because through its own actions, and those of Congress, emerging competition itself will discipline rates and remove cable firms from regulatory rate supervision. Moreover, the investment cycle may be different for each franchise or system, and would vary according to the timing of rebuilds, remaining franchise life, and market conditions.

As a consequence of these limiting factors, the Commission needs to reconsider its apparent disinclination to use a risk premium approach. Lenders may be counted on to properly appraise the actual risks of investment in cable. By adopting a risk premium approach, and prescribing an equity return greater than the debt cost, the Commission will (a) accurately map the actual financial risks of cable, (b) simplify its rate process, and (c) assure just compensation.

## **V. OTHER RATEMAKING ISSUES**

### **A. Cost Allocation**

The Commission also suggests (NPRM ¶ 11) that cost of service, like benchmarks, should carry forward the principles of "tier neutrality." Whatever may be said in defense of applying the same benchmark price to basic and tier channels, one cannot say that it is cost-based. When adopted, "tier neutrality" was

offered as a simplifying instruction which combatted a feared tendency to retier basic signals into a more expensive tier. It was not based on considerations of cost.

A closer view of cost causation reveals many costs which are not "tier neutral." For example, cable's costs for programming services are undeniably greater, channel-for-channel, than the costs of basic service. Cable programming service tiers carry sizable program license fees. By contrast, the programming costs for basic service are comparatively less.

As systems mature, allocations based on number of subscribers become easier to implement, but channel-based allocations will be skewed by digital compression. The Commission could develop a subscriber-weighted allocator weighted for actual household subscription levels so that channels devoted to relatively few subscribing households would not bear a disproportionate share of costs. Over time the Commission will be able to better develop the sense of cost allocation and establish acceptable methodologies. Until that time, cable operators should be permitted to elect -- as appropriate -- the methodology best suited to reflecting cost causation.

Blindly applying "tier neutrality" concepts would also undermine the preference for allocating costs according to cost causation. 47 C.F.R. § 76.624(f). As to common costs which cannot be allocated by causation, the Commission should take care

not to limit allocation only in proportion to the number of channels on the tier, however appealing its simplicity.

An analysis of cost causation for a cable system reveals at least two predominant factors which drive cost: the number of channels designed in the system and the number of subscribers. However, neither of these factors is clearly superior to the other. What is clear is that neither factor has any apparent direct relationship to the other and thus are mutually exclusive. Thus, employment of either factor in isolation will forego the influence of the other. In the transition stage, the Commission should avoid mandating inflexible methods of cost allocation among tiers. Cable operators should be allowed to select the most appropriate method.

However, if the principle of "tier neutrality" is intended to require that cost of service showings be made both at the FCC and municipal level, then the Commission's suggestion is even more greatly flawed. There is no fundamental reason that the Commission should not permit a franchising authority to approve a benchmark rate while the Commission considers a cost-of-service showing for cable programming services. The Commission has already stated that an operator is permitted to charge less than the maximum rate, and (assuming rational behavior) benchmarks may be assumed to be beneath the cost-of-service rate pursued by an operator. Jurisdictional divisions are also



commonplace in telephone regulation. For example, the Commission has accepted the fact that under Section 2(b) of the Communications Act, state PSCs may prescribe different depreciation rates than does the FCC, for the same physical plant.<sup>77/</sup> For another example, the Commission has never suggested that a LEC would be prohibited from following Commission price caps for interstate access if the state PSC continued to apply rate of return regulation to intrastate service. In implementing the Cable Act, the Commission has taken pains to permit franchising authorities to decline to certify in order to follow less formal ratemaking methods. It would be irrational to deny a cable operator the right to pursue cost of service for the cable programming service merely because a local franchising authority has declined to certify or has not chosen to conduct a cost of service case.

The Commission has also suggested that tier neutrality is a prophylactic measure to prevent undue incentives to move cable networks from basic to the satellite tier. Even assuming that the Commission is right in its reading of Congressional intent, this "tier neutral" solution is unnecessary and counterproductive. If the Commission is concerned that basic service will be artificially stripped in order to pad the satellite tier ratebase, it may adopt reasonable rules to limit costs which it deems to have been artificially imposed. It could, for

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<sup>77/</sup> See Louisiana Pub. Serv. Comm'n, 476 U.S. at 355.